Internal Revenue Service

memorandum

date: SEP 26 1991

to: Director, Internal Revenue Service Center
Kansas City, MO
Attn: Entity Control

from: Technical Assistant
Employee Benefits and Exempt Organizations

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subject: CC:EE:3 - TR-45-1385-91
Railroad Retirement Tax Act Status

Attached for your information and appropriate action is a copy of a letter from the Railroad Retirement Board concerning the status under the Railroad Retirement Act and the Railroad Unemployment Tax Act of:

[redacted]

We have reviewed the opinion of the Railroad Retirement Board and, based solely upon the information submitted, concur in the conclusion that [redacted] is an employer covered under the Railroad Retirement Act and the Railroad Unemployment Insurance Act effective [redacted], the date it began operations. It should file Forms CT-1 and Forms 941-E for the appropriate periods.

(Signed) Ronald L. Moore

RONALD L. MOORE

Attachment:
Copy of letter from Railroad Retirement Board

08903

cc: Mr. Gary Kuper
Internal Revenue Service
200 South Hanley
Clayton, MO 63105

UNITED STATES OF AMERICA
RAILROAD RETIREMENT BOARD
844 RUSH STREET
CHICAGO, ILLINOIS 60611

BUREAU OF LAW

Assistant Chief Counsel
(Employee Benefits and
Exempt Organizations)
Internal Revenue Service
1111 Constitution Avenue., N.W.
Washington, D.C. 20224

AUG 09 1991

Attention: CC:IND:1:3

Dear Sir:

In accordance with the coordination procedure established between the Internal Revenue Service and this Board, I am enclosing for your information a copy of an opinion in which I have expressed my determination as to the status under the Railroad Retirement and Railroad Unemployment Insurance Acts of the following:

[redacted]

Sincerely yours,

Steven A. Bartholow
Deputy General Counsel

Enclosure

FORM G-115f (11-89)

UNITED STATES GOVERNMENT

MEMORANDUM

RAILROAD RETIREMENT BOARD

[redacted]

JUL 29 1991

TO: Director of Research and Employment Accounts

FROM: Deputy General Counsel

SUBJECT: [redacted]
Employer status

This is in response to your Form G-215 dated November 5, 1990, requesting my opinion as to the employer status of [redacted] (hereafter [redacted]) under the Railroad Retirement and Railroad Unemployment Insurance Acts (hereafter the Acts).

In an enclosure to a letter dated [redacted], from [redacted], attorney for [redacted], the following information was provided. [redacted] was incorporated on [redacted] and began operations on that date. The chief executive officer of [redacted] is [redacted], who is its sole shareholder. [redacted] is also a shareholder, director and officer of several railroad carriers. Those carriers and the percentage of his ownership therein are as follows:

[redacted] ([redacted]% common interest)
[redacted] ([redacted]% common interest)
[redacted] (indirect common interest through [redacted]% interest in corporate parent [redacted])
[redacted] ([redacted]% common interest)
[redacted] ([redacted]% common interest)
[redacted] ([redacted]% common interest)1/

[redacted] is a director and principal officer of [redacted] and the [redacted] and [redacted], [redacted]. [redacted] is a principal officer of [redacted] and each of the carriers listed. In addition, she is a director of the [redacted] and the [redacted]. According to the Pocket List of Railroad Officials, [redacted] is the President of the [redacted], [redacted], [redacted], and the [redacted].

1/ These carriers have all been held to be employers under the Acts. See Legal Opinions [redacted] and [redacted] respectively.

Director of Research and Employment Accounts

According to the enclosure to [redacted]'s letter "[T]he officers of [redacted] provide a wide variety of consulting services including advice regarding operational problems, financial analysis, personnel issues, marketing developments and general management concerns. The employees of [redacted] provide accounting and clerical services."

The enclosure to [redacted]'s letter also stated as follows:

"[redacted] offers its services to the public at large. [redacted]'s clients outside the railroad industry include a trucking company, a real estate company, leasing companies, law firms and other private industries."

Finally, in response to a question about [redacted] & [redacted]'s revenues, the enclosure provided the following information:

"[redacted]

[redacted] REVENUE ANALYSIS

		REVENUE PERCENTAGE	RAIL PERCENTAGE
[redacted] RAIL REVENUES:			
[redacted]	$[redacted]	[redacted]%	[redacted]%
[redacted]	$[redacted]	[redacted]%	[redacted]%
SUBTOTAL	$[redacted]	[redacted]%	[redacted]%
[redacted] NONRAIL REVENUES	$[redacted]	[redacted]%	0.00%
TOTAL REVENUE	$[redacted]	[redacted]%	[redacted]%

2/ [redacted] has been held to be an employer under the Acts (see Legal Opinion [redacted]). [redacted]'s letter did not state that [redacted] was a shareholder in it, but at the time [redacted] was issued [redacted] was the General Manager of that railroad. In the Pocket List of Railroad Officials, 1st Qtr [redacted], [redacted] is no longer shown as an officer.

Director of Research and Employment Accounts

The percentages shown under "REVENUE PERCENTAGE" are the percentages of [redacted]'s revenues attributable to each railroad and to nonrail revenues. The percentages under "RAIL PERCENTAGE" appear to be the percentages of [redacted]'s revenues discounted to reflect [redacted]'s ownership interest in each railroad. Total revenues from the affiliated railroads total $[redacted], or [redacted] percent of the total revenues for [redacted] in [redacted].

Section 1(a)(1) of the Railroad Retirement Act (45 U.S.C. § 231 (a)(1)) provides in pertinent part as follows:

> "The term "employer" shall include--
> (i) any express company, sleeping-car company, and carrier by railroad, subject to part I of the Interstate Commerce Act;
>
> (ii) any company which is directly or indirectly owned or controlled by, or under common control with, one or more employers as defined in paragraph (i) of this subdivision, and which operates any equipment or facility or performs any service (except trucking service, casual service, and the casual operation of equipment or facilities) in connection with the transportation of passengers or property by railroad * * *"

A similar provision is contained in section 1(a) of the Railroad Unemployment Insurance Act (45 U.S.C. § 351(a)).

The Board has by regulation set forth guidance with respect to the meaning of the terms "control" and "common control." Those regulations provide as follows:

> "§202.4 Control.
>
> A Company or person is controlled by one or more carriers, whenever there exists in one or more such carriers the right or power by any means, method or circumstance, irrespective of stock ownership to direct, either directly or indirectly, the policies and business of such a company or person and in any case in which a carrier is in fact exercising direction of the policies and business of such a company or person.
>
> §202.5 Company or person under common control.

Director of Research and Employment Accounts

> A company or person is under common control with a carrier, whenever the control (as the term is used in § 202.4) of such company or person is in the same person, persons, or company as that by which such carrier is controlled."

The power of control "need not be exercised in some affirmative, spectacular manner in order to amount to actuality of control". Universal Carloading & Distributing Co. v. Railroad Retirement Board, 172 F. 2d 22,26 (D.C. Cir. 1948).

It is clear that [redacted] is not a carrier by railroad. However, [redacted] is the president and a director of several railroad carriers. He also has substantial stock ownership in several railroad carriers, including a controlling interest in two of them. Moreover, other principal officers of [redacted] are also officers and directors of those rail carriers. Based on these facts, I conclude that [redacted] is under common control with those affiliated rail carriers. Utah Copper Co. v. Railroad Retirement Board, 129 F. 2d 358,363 (10th Cir., 1942).

Nevertheless, this is only the first part of the test set forth in section 1(a)(1)(ii). Since it is not itself a carrier by rail, in order to be found to be an employer under the Acts [redacted] must, in addition to being under common control with one or more railroad employers, be performing "services in connection with the transportation of passengers or property by railroad."

The question of what constitutes "services in connection with the transportation of passengers or property by railroad" has been litigated on several occasions. In Adams v. Railroad Retirement Board, 214 F. 2d 534 (9th Cir. 1954), the Court held that the provision of "accounting services, the services of a purchasing department, * * * correspondence and stenographic services * * * bridge and building services, a safety engineer and repairs for its automotive equipment and its general rolling stock" by a carrier's affiliate were services in connection with rail transportation so as to render the affiliate an employer under the Acts. Adams, at 542. In Southern Development Co. v. Railroad Retirement Board, 243 F. 2d 351 (8th Cir. 1957), the Court, at 355, held that a railroad affiliate which owned and operated an office building "almost exclusively for use by a railroad company for ticket selling and general offices could reasonably be considered [to be performing] a service connected with and supportive of rail transportation" and was an employer

Director of Research and Employment Accounts

under the Acts. In Railroad Concrete Crosstie Corp. v. Railroad Retirement Board, 709 F. 2d 1404 (11th Cir. 1983), the Court held that the provision of crossties by a manufacturer to its railroad carrier affiliate was "supportive of transportation and essential to its proper functioning." Railroad Concrete Crosstie, 709 F. 2d at 1410, quoting Southern Development Co. Consequently, the manufacturer of crossties was an employer under the Acts.

In Itel Corp. v. United States Railroad Retirement Board, 710 F. 2d 1243 (7th Cir. 1983), the court held that the leasing of rail cars is not a service in connection with the transportation of passengers or freight by rail. The Seventh Circuit read section 1(a)(1)(ii) of the Act as applying to services covered by the Interstate Commerce Act or where the related entity exists to serve the rail carrier affiliates and where its primary purpose is to remove employees from coverage under the Railroad Retirement Act. Itel, at 1248.

In a later decision, Standard Office Building Corporation v. U.S., 819 F. 2d 1371 (7th Cir. 1987), the Seventh Circuit was somewhat critical of its reading of section 1(a)(1)(ii) in the Itel decision. The Seventh Circuit stated that:

> "Our attempt to yoke together the Interstate Commerce Act and the railroad retirement acts overlooked, however, the asymmetry of the regulatory schemes. Suppose a railroad spun off all its brakemen into a subsidiary. Although the function performed by the brakemen would not be directly subject to the Commission's price and service regulation, because it wouldn't be a carrier service--that is, a service sold to shippers or passengers--there would be indirect regulation, because the ICC can always disallow improvidently incurred costs of service.
>
> * * * * *
>
> "Thus there was no need to interpret the words performs 'all services in connection with' rail transportation in the Interstate Commerce Act (49 U.S.C. § 1(3)(a), repealed in 1980) to reach services not directly regulated by the ICC: those services were subject to indirect regulation. But if a railroad could avoid railroad retirement tax by spinning off its brakemen into a subsidiary which then sold their services back to the railroad and not to the shipping

> public, so that these services were not regulated by the ICC in the sense used in ITEL, this would be a massive evasion of the railroad retirement acts, for there is no indirect regulation of retirement. That is why the court in ITEL added the second step of its analysis: even if the service performed by the affiliate is not a (directly) regulated service, it is subject to those acts if the intent is to undermine them. Really the whole weight of the analysis falls on the second step, which by making intent the central issue injects an undesirable element of uncertainty into the administration of the railroad retirement acts." 819 F. 2d, at 1378.

In refusing to accept the argument of Standard Office Building Corporation that section 1(a)(1)(ii) of the Act applies only to "the 'direct' performance of railroad service by operating employees," the Seventh Circuit stated that:

> "The distinction is unrelated to the purpose of the statute because the words 'performs any service ... in connection with [rail] transportation' were intended to exclude services unrelated to rail transportation, such as operating an amusement park open to the public on land owned by the railroad, rather than to make a hair-splitting distinction between workers who 'really' run the railroad and those who back up the former group. The Act covers 'substantially all those organizations which are intimately related to the transportation of passengers or property by railroad in the United States.' S.Rep. No. 818, 75th Cong., 1st Sess. 4 (1937). This would describe a wholly owned subsidiary to which a railroad spun off its entire nonoperating staff." Id., at 1376.

The court in Standard Office Building concluded that the best approach to resolving questions as to whether a service performed by an affiliated entity is a service in connection with rail transportation "is one that will minimize corporate reorganization designed to avoid railroad retirement tax liability and will protect reasonable expectations." Id., at 1379. In making its determination, the Seventh Circuit looked to the history of the entity (which was formed 35 years before enactment of the Railroad Retirement Tax Act), the situation and expectations of the employees (they were not members of railway labor organizations), and the degree to which the affiliate services the rail carrier affiliate(s). Id., at 1379-1380.

Director of Research and Employment Accounts

After holding that Standard Office Building was not a covered employer, the court specifically declined to express an opinion as to whether its holding would have been different had the company not been formed 35 years prior to enactment of the Railroad Retirement Tax Act or if the percentage of the rail affiliate's occupancy in the building been higher than the 42-57 percent range in the years in question. Id., at 1380.

According to the enclosure to [redacted]'s letter, [redacted] provides accounting and clerical services, general consulting services and advice regarding operational problems, personnel issues, marketing and general management concerns to the rail carriers enumerated above. The contracts for services are of a general nature and are automatically renewed on a yearly basis. The cases reviewed above hold that a railroad affiliate which is performing a service necessary to railroad transportation is performing a "service in connection with" railroad transportation. The accounting and clerical services provided by [redacted] are the same services held to be "service in connection with" in Adams. The advice on operational problems, personnel issues, marketing and general management concerns are all services [redacted] provides to its affiliates to enable the affiliates and [redacted] to act so as to maximize its return on its investments. These are all services which are intimately related to railroad transportation and which the railroad affiliates could perform for themselves but have chosen to have [redacted] perform on their behalf.

It is also significant that unlike the railcar leasing operations at issue in Itel, a substantial portion of the business of [redacted] is with its affiliated railroads. In [redacted], [redacted] percent of [redacted]'s revenues were attributable to its railroad affiliates. By contrast, in Itel, only 11 percent of Itel Rail Division's business was with its affiliated rail carriers.

Based on the above discussion of the facts and precedent case law, I conclude that the services being performed by [redacted] for its rail carrier affiliates are "services in connection with the transporation of passengers or property by railroad," and since the services in question generate two-thirds of [redacted]'s total revenues on an annual basis, those services are not casual service. Casual service is defined by Board regulation (20 CFR 202.6) as service which is "so irregular or infrequent as to afford no substantial basis for an inference that such service * * * will be repeated, or whenever such service * * * is insubstantial." Given the relationship between [redacted], its officers and directors, and the railroads cited in this opinion and the large portion of its revenue which is derived by [redacted] from the railroad industry, this service cannot be considered to be casual under the Board's regulations.

Director of Research and Employment Accounts

Since [redacted] meets the definition of an employer contained in the Acts, it is my determination that it is an employer covered under the Acts. [redacted] began operations on [redacted] and has been an employer since that date.

An appropriate G-215 giving effect to this determination is attached.

Steven A. Bartholow

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